

Silverwood Industries Annual Report

AR21



Financial highlights

Year ended December 31, 1978 and January 1, 1978	1978	1977
Sales	\$294,341,803	\$265,866,529
Income before extraordinary item	\$ 1,517,658	\$ 561,926
Net income for year	\$ 1,517,658	\$ 2,086,126
Earnings per Class "A" and "B" shares		
Income before extraordinary item	\$ 1.13	\$.42
Net income for year	\$ 1.13	\$ 1.55
Dividends paid	\$ 806,620	\$ 806,620
Rate per Class "A" and "B" shares60	.60
Retained earnings re-invested in business to date	\$ 22,195,614	\$ 21,484,576
Shareholders' equity	\$ 29,536,931	\$ 28,825,893
Shares outstanding		
Class "A"	903,158	903,158
Class "B"	441,212	441,212
Equity per Class "A" and "B" share	\$ 21.97	\$ 21.44
Debentures outstanding	\$ 5,175,500	\$ 5,597,000
Funds from operations	\$ 5,250,062	\$ 4,024,528
Working capital	\$ 7,631,421	\$ 6,710,906

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Annual Meeting

May 3, 1979 — 2:00 p.m.
London, Canada

75th Anniversary



A. E. Silverwood (1876-1961)



E. G. Silverwood (1904-1972)

Ten year comparative summary

Fiscal year	1978	1977	1976
Sales	\$294,341,803	265,866,529	238,234,978
Income before extraordinary item	\$ 1,517,658	561,926	559,057
Net income for year	\$ 1,517,658	2,086,126	2,153,708
Income for each Class "A" and "B" share before extraordinary item	\$ 1.13	.42	.42
Net income for each Class "A" and "B" share for year	\$ 1.13	1.55	1.60
Dividends	\$ 806,620	806,620	1,008,277
Per Class "A" share	\$.60	.60	.75
Per Class "B" share	\$.60	.60	.75
Percentage of consolidated earnings paid in dividends	53.1%	38.7%	46.8%
Earnings re-invested in the business	\$ 711,038	1,279,506	1,145,431
Percentage of earnings re-invested in the business	46.9%	61.3%	53.2%
Capital invested	\$ 12,766,003	14,212,419	14,903,941
Long term debt	\$ 29,536,931	28,825,893	27,546,387
Shareholders' equity	\$ 42,302,934	43,038,312	42,450,328
Total	\$ 42,302,934	43,038,312	42,450,328
Percentage of shareholders' equity to total investment	69.8%	67.0%	64.9%
Shareholders' equity per share	\$ 21.97	21.44	20.49
Working capital	\$ 7,631,421	6,710,906	8,179,863

1978 — Fifty-two weeks ended December 31, 1978
1977 — Fifty-three weeks ended January 1, 1978
1972-76 — Fifty-two weeks ended approximately the end of December in each year
*1972 — Fifty-two weeks ended January 2, 1972
1971 — Forty weeks ended January 3, 1971
1970 — Twelve months ended March 31, 1970

1975	1974	1973	1972	*1972	1971	1970
261,326,735	229,080,262	189,207,993	172,001,680	162,629,505	118,042,541	144,678,893
1,881,886	1,354,921	2,204,189	1,247,582	1,504,587	1,409,910	1,885,299
2,306,639	1,645,750	2,452,100	1,762,700	1,538,348	1,466,225	2,261,507
1.40	1.01	1.64	.93	1.12	1.05	1.40
1.72	1.22	1.82	1.31	1.14	1.09	1.68
1,075,496	1,075,496	1,075,496	1,075,496	1,075,496	806,622	1,075,498
.80	.80	.80	.80	.80	.60	.80
.80	.80	.80	.80	.80	.60	.80
46.6%	65.3%	43.9%	61.0%	69.9%	55.0%	47.6%
1,231,143	570,254	1,376,604	687,204	462,852	659,603	1,186,009
53.4%	34.7%	56.1%	39.0%	30.1%	45.0%	52.4%
13,440,267	13,149,557	12,104,719	12,684,757	11,007,652	10,670,617	10,696,847
26,400,956	25,169,813	24,599,559	23,222,955	22,535,751	22,072,899	21,413,296
39,841,223	38,319,370	36,704,278	35,907,712	33,543,403	32,743,516	32,110,143
66.3%	65.7%	67.0%	64.6%	67.1%	67.4%	66.7%
19.64	18.72	18.30	17.27	16.76	16.42	15.93
5,110,055	2,671,837	3,339,964	3,929,331	3,274,310	3,355,441	4,249,573

Board of Directors

Silverwood Industries Limited

Directors

(as at December 31, 1978)

W. I. Barton*
London, Ontario
G. M. Carlyle
Calgary, Alberta
Eric F. Findlay†*
Toronto, Ontario
A. E. Lawrence, Jr.
London, Ontario
R. G. Pardy*
London, Ontario
W. Sagain
Toronto, Ontario
D. G. Silverwood†*
Chairman
Silvertree Realty Inc.
Palm Springs, Cal.
W. A. Stewart
London, Ontario
J. Allyn Taylor†*
Honorary Chairman
The Canada Trust Company
and the Canada Trustco
Mortgage Company
London, Ontario
D. H. Thain†*
Professor, School of
Business Administration,
University of Western Ontario
London, Ontario
C. L. Tulloch
London, Ontario
D. B. Weldon†*
Chairman of the Board
Midland Doherty Limited
Toronto, Ontario

Honorary Directors

A. E. Lawrence, Sr.
London, Ontario
H. T. Spettigue
London, Ontario

†Member of the Audit Committee

*Member of the Executive Committee

Officers

Eric F. Findlay
Chairman of the Board,
President and
Chief Executive Officer
R. G. Pardy
Vice President, Finance
G. R. Carton
Vice President,
Legal & Corporate Af-
fairs
W. Sagain
Vice President,
Corporate Development
R. S. Maich
Vice President
W. I. Barton
Secretary-Treasurer
A. E. Lawrence, Jr.
Assistant Treasurer
N. W. Sanderson
Assistant Secretary

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To Our Shareholders

The principal purpose of my report this year is of course to review the financial records and activities of the past year but more importantly to give you a sense of the future direction of management and the controlling shareholders of your company. Over the past six or seven years, the Company has been in a phase of re-direction. The main goal was the restoration of the historical earning levels of the Company. Equally important was the establishment of management policies, systems and organization to build a firm foundation for growth. We believe that meaningful progress has been made toward this end and that Silverwood Industries is better positioned for the future.

Rationalization of the Ontario Dairy segment remains a key priority. The inflationary period of the "70's" combined with rapidly escalating energy costs, has had a profound impact on the operating techniques within the industry. These factors, together with the geography of Canada, are bringing about an increasing concentration of strength in the food retailing sector. This has dramatically affected Silverwood's ability to bring its products to the attention and choice of the Canadian consumer. Historically, we have marketed our products through Home Service delivery and local independent retailers. It was a natural evolution from Home Service to marketing through Convenience Stores while continuing our strong concentration with the local retailer. However, as consumer's buying habits change this retailer segment has been gradually declining, while the market share of the large supermarkets has been substantially increasing.

Convenience store sales have been shifting markedly from the emphasis on commodity products such as milk, ice cream, bread, soft drinks, tobacco and grocery staples of a decade ago. Changing life styles within our community are influencing the product make-up of these stores with milk and bread now forming a smaller percentage of total sales.

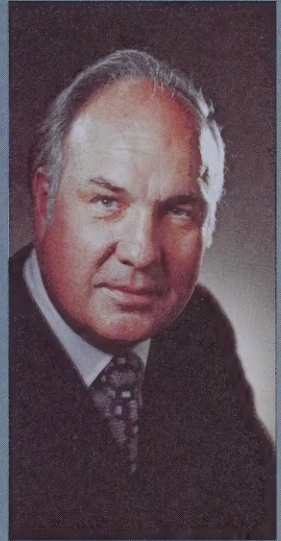
To Our Shareholders

Thus for the Dairy Division, the last decade has been a constantly changing market position and one which has made consistent profitability an elusive goal. However, for our Convenience Store Division, it has provided a challenging medium for dramatic growth and opportunities for increasing profit through meeting the changing needs of society.

The one overriding principle which has been followed over these past few years and which continues to be followed in the decisions in each of our operating divisions, is that each decision made includes consideration of the long term view. We intend to manage not only for today's profit but for tomorrow's potential.

This year your Company has celebrated its 75th year of operations. It is a rather remarkable achievement and one which is emulated by few in this country of ours. Anniversaries tend to make us reminisce. As individuals, they allow us the luxury of remembering past achievements and successes, of reviewing failures and disappointments tempered by time. Within the Silverwood corporate family, there are some 155 active employees with 25 years service or more making their personal contribution each day to the growth and success of the Company to which they have dedicated their working lives. In addition, there are some 303 retired staff as members of the Silverwood Pension Plan who have devoted at least 25 years of their lives to the success and stature attained by Silverwood within those 75 years. It is with pride that we record that there have been 749 employees in all serve the Company 25 years or more. These people view with a great personal pride the record of achievement of this Canadian Company.

It is appropriate in celebrating 75 years of service to the community that acknowledgement be given to the strong entrepreneurial leadership provided in the building of this leading Canadian Company by the Silverwood family. A.E. (Bert) Silverwood and his son, E.G. (Gordon) Silverwood,



*Eric F. Findlay
Chairman of the Board
President and
Chief Executive Officer*

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To Our Shareholders

between them served at the helm of the Company for 65 of the 75 year history. It was their courage, foresight and ingenuity that developed and led this Company into the strong Canadian entity it is today. In 75 years, there are many individuals who contributed in major ways at various levels of the organization. Among them, we want to mention and thank J. Harold Gillies, J.H. Duplan, Erie B. Nelles, Max R. McCrea, Norman E. Kaye, Leslie R. Gray, R.G. (Bob) Peat, T.L. Davies, H.E. (Bert) Spettigue, C.L. (Liv) Tulloch and Donald G. Silverwood.

1978 marks as well, a change in the controlling shareholders of Silverwood. On September 29th, Silverwood Investors Limited (the Silverwood family holding company which owned 42.3% of Class "B" Voting shares of Silverwood) was purchased by nine Executives of Silverwood under the name Execsil Corporation. Royal Oak Dairy Limited, a controlled subsidiary of Silverwood was purchased at the same time and the three companies — Investors, Royal Oak and Execsil have subsequently been merged to form Execsil Corporation.

The Silverwood family has seen fit to purchase approximately 10% of the equity of Execsil. Dorothy M. Lawrence, the daughter of A.E. Silverwood and sister of Gordon, gave leadership to these undertakings to ensure the continuity of this great Canadian Company. The Silverwood Company is proud of its Canadian heritage, and Management is determined to continue its great Canadian tradition.

Before outlining the commitments of Silverwood Management in developing improved financial returns in the future, I want to review with you the significant events of this past year.

Our overall sales growth has been most acceptable with consolidated net sales of \$294,341,803, showing an increase of \$28,475,274 over those of 1977. It should be noted that with period accounting, 1977 was a 53 week fiscal year while 1978 was only 52 weeks in length. A break-out of sales within the Divisions, and before intercompany consolidation, records Silverwood Dairies with sales of \$129,978,591, an increase of 7.6% or \$9,226,025 over the previous year. Mac's Convenience Stores Limited attained an overall sales record of \$166,710,297, an excellent increase of \$20,009,146, or 13.6% over 1977.

In 1978, Silverwood took some very affirmative steps towards profit levels consistent with the Company's expanding revenue base. Consolidated net income from operations of \$1,517,658, or \$1.13 per class of "A" and "B" Share increased \$955,732, or 71.1c per share over the earnings reported in our 1977 fiscal year. There were no extraordinary earnings recorded during the 1978 fiscal year. This is a marked improvement for our Shareholders over the previous two years and should indicate a return to more realistic earnings for the Company.

Within the Divisional segments of our total operations, much has been accomplished and is ongoing for the future potential earnings of Silverwood.

The momentum of Mac's Convenience Stores and its leadership of the Canadian convenience store industry, provides a foundation for continued profitable growth within the existing store base, continued growth in Canadian markets through the acquisition of new locations, and a potential for growth via acquisition into the United States and possibly other International markets.

To Our Shareholders

Mac's are concentrating on adding new services and products which their customers seek rather than assuming that existing services and products are adequate in their current form. They have demonstrated a responsiveness to the changing needs of consumers and an ability to assess and anticipate the future needs of the public. Mac's management has emphasized a return on investment growth and market share growth in both existing and new stores rather than simply achieving growth through new store addition.

Baskin-Robbins management, although a much smaller entity, is growing rapidly and has developed within its store franchisees an esprit de corps that is both unusual and refreshing in the retail franchise field today. They merchandise fun and enjoyment through their ice cream marketing program and have great growth and profit potential in what otherwise tends to be a static growth market. Negotiations and agreements were completed in December, 1978 with Baskin-Robbins Incorporated of California to extend the Silverwood franchise from Ontario to encompass all of Canada. It is anticipated that Baskin-Robbins will enter both the British Columbia and Quebec markets in latter 1979.

Silverwood Dairies, during these last two years, has placed great emphasis upon the development of an aggressive, knowledgeable, cost conscious management team capable of making a significant contribution in the re-structuring of our Dairy business. They have been encouraged to develop a highly de-centralized management team much more responsive to the needs of the Consumers. While still too early to predict a return to satisfactory investment returns, the Dairies management group is committed to establishing a proper return through cost efficiencies, growth and rationalization of operations where necessary.

In the area of management commitments, there are certain fundamental principals and strategies to which Silverwood management is dedicated in the re-establishment of a sound financial return to its Shareholders.

- Of all the Company's objectives and strategies, none is more important than the realization that people are what truly makes the difference. Your Management is totally committed and dedicated to the development of quality and depth in management. It has been a strength of Silverwood through 75 years. We are committed to the development and use of training programs within our retailing network for store supervision, dealers and franchisees.
- Every emphasis will be placed on the development of opportunities for our people. Management firmly believes in the philosophy of encouragement of entrepreneurial activity and the economic strength that it generates, not only for the Company but for the whole Canadian economy. Our total retailing program in Mac's and Baskin-Robbins is based on allowing the individual to use his own ingenuity and strength in establishing his position and making his contribution to society.
- The company has been moving rapidly in all of its Divisions these past three years to a de-centralized operating management philosophy. This policy in our opinion, provides the best environment for maintaining high levels of individual motivation and performance. The policy promotes more informed decisions and develops

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To Our Shareholders

more rapid responses to capitalize on opportunities in the marketplace.

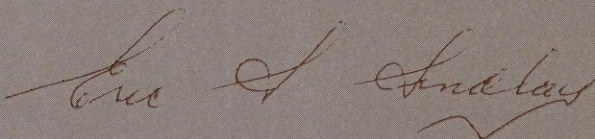
- Management is committed to the maintenance of quality in our processing operations. Silverwood has developed an enviable reputation in the Canadian marketplace over many years for the premium quality of its products, and it has not allowed the pressures of the inflationary economy to change that objective as we see happening in so many other situations.
- Silverwood management is committed to growth and the positioning of its Divisions within the marketplace so that they are capable of growth internally. As well, we are consistently looking for acquisitions compatible with our many operating strengths. There are few companies that have the depth of management experience in food processing technology, specialty store retailing, real estate leasing and development and franchising that is encompassed within Silverwood.
- Management is committed to flexibility within our invested capital base. With the rapidly changing needs and direction of society, we intend to strive for that flexibility which allows for changing direction of capital investment as the economy dictates.
- While we are not in an active divestment posture today, management has already demonstrated that part of our operational philosophy is to divest in those areas of business which have marginal position and a limited earnings potential. Although we are fully cognizant of tradition and the Company heritage so ably provided over 75 years, we must focus on the potential of the future for our people and our shareholders.
- With the change of control of the Company being placed in management hands, we are committed to a strengthening of our Board of Directors with greater representation from external people. We want to assure our Class "A" Shareholders of competent representation and together with management to aggressively pursue the full development of our potential.
- Management is totally committed to the development of a strong Canadian entrepreneurial business institution within a unified, vibrant and growing Canada.

While acknowledging that there still remains a re-focusing in parts of our Dairy operations, the outlook for Silverwood, in its full scope, is most encouraging.

I want to express my sincere personal appreciation to your Board of Directors and particularly its external Directors, for their interest, support and dedicated service to the Company during this last year. They exercise their franchise to represent all Shareholders of Silverwood in a most commendable fashion and I can but comment that the Shareholders of Silverwood have been most fortunate in having such a dedicated group represent them.

The commitments to fundamental principles and strategies for the future are designed to build upon the many strengths that are already inherent within the Silverwood entity and its loyal people base. We are confident that the aggressive and competent management team within Silverwood is capable of creating and producing a dedicated contribution to the Canadian entity and an exciting and financially rewarding future.

We look forward with enthusiasm to meeting our new challenges.



Chairman of the Board
President and
Chief Executive Officer

Financial Year in Review

The 1978 fiscal year of Silverwood Industries Limited and its subsidiaries comprises 52 weeks ended December 31, 1978. Royal Oak Dairy, Limited is included in the consolidated statements of income and changes in financial position, reflecting operations for 1978, from January 1, 1978 to the date of sale on September 29, 1978, and for the whole year in the comparative amounts for 1977.

As of September 29, 1978, the Company disposed of its investment in Royal Oak at its carrying value of \$2,050,000. This transaction provided an improvement in working capital of \$785,049.

Sales and income

Operating earnings of \$1,517,658 in 1978 represent \$1.13 per share, compared with \$561,926 or \$0.42 per share in 1977. Silverwood Dairies was unprofitable for the third consecutive year, but the loss was reduced from that experienced in 1977. The convenience store division continued to provide satisfactory results, with 1978 earnings in excess of those of 1977.

There was no extraordinary income from sale of business segments or redundant properties in 1978. Consequently, total earnings this year at \$1.13 per share were lower than 1977 at \$1.55 per share. Extraordinary items in 1977 amounted to \$1,524,200 or \$1.13 per share.

Royal Oak Dairy, Limited earnings are included in 1978 operating earnings in the amount of \$177,208, representing the equity held by Silverwood Industries Limited for nine months from January 1, 1978 to September 29, 1978.

Annual consolidated sales for 1978 were \$294,341,803, compared with \$265,866,529 in 1977, an increase of 10.7 per cent. A comparative breakout of sales for the two year period is as shown in the table following.

1978

SALES SUMMARY

	1978	1977	Per Cent Change
Dairies Division — Silverwood Dairies	\$129,978,591	\$120,752,566	7.6
Convenience Store Division			
Mac's Convenience Stores	166,710,297	146,701,151	13.6
	296,688,888	267,453,717	10.9
Consolidated sales of Royal Oak Dairy, Limited (1978 — January 1, 1978 to September 29, 1978)	15,539,208	19,263,096	(19.3)
All Other	5,318,139	4,321,428	23.1
Total	317,546,235	291,038,241	9.1
Inter-company sales	23,204,432	25,171,712	(7.8)
Total consolidated sales	\$294,341,803	\$265,866,529	10.7

Cost of sales as a percentage of sales decreased from 78.77 to 77.55, a decrease of 1.22 per cent, while selling, administrative and general expenses increased by .89 per cent from 18.72 per cent in 1977 to 19.61 per cent in 1978. Depreciation and amortization expense decreased from \$4,067,602 in 1977 to \$4,033,604 in 1978; this represents a percentage of sales decrease from 1.54 per cent in 1977 to 1.37 per cent in 1978.

Capital Expenditures

Of the fixed asset additions of \$3,944,716 (\$4,986,615 in 1977), the largest category of expenditure of \$1,563,000 represented new store openings and renovations in the Convenience Store division. There were no significant capital projects in the Dairies division. The balance of capital items largely represented plant replacement, delivery and merchandising equipment.

Balance Sheet Position

The Company's balance sheet continued to improve in 1978 despite lower total earnings. Working capital improved by \$0.9 million to \$7.6 million while long term debt was reduced from \$14.2 million to \$12.8 million. Short term bank loans were also reduced. The equity per share at year-end stands at \$21.97 and the debt to equity ratio (excluding deferred taxes), is 1 to 2.31.

Auditors' report

To the Shareholders of Silverwood Industries Limited.

We have examined the consolidated balance sheet of Silverwood Industries Limited as at December 31, 1978 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination of the financial statements of Silverwood Industries Limited and those subsidiaries of which we are the auditors was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances. We have relied on the reports of the auditors who have examined the financial statements of Royal Oak Dairy, Limited and its wholly owned subsidiaries.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

London, Canada.
February 28, 1979.

Clarkson, Gordon & Co.
Chartered Accountants.

Consolidated statement of income

YEAR ENDED DECEMBER 31, 1978 (with comparative amounts for the year ended January 1, 1978)	December 31, 1978	January 1, 1978
Sales	\$294,341,803	\$265,866,529
Less:		
Cost of sales	228,257,996	209,433,155
Selling, administrative and general expenses	57,705,730	49,800,893
Depreciation and amortization	4,033,604	4,067,602
Interest — short-term debt	467,111	290,126
— long-term debt	1,131,404	1,306,527
	291,595,845	264,898,303
Income before taxes, minority interest and extraordinary item	2,745,958	968,226
Taxes on income (note 10):		
Current	1,529,500	1,011,300
Deferred	(392,200)	(754,300)
	1,137,300	257,000
Income before minority interest and extraordinary item	1,608,658	711,226
Minority interest	(91,000)	(149,300)
Income before extraordinary item	1,517,658	561,926
Extraordinary item (note 7)		1,524,200
Net income for year (note 1(a))	\$ 1,517,658	\$ 2,086,126
Earnings per Class "A" and "B" shares:		
Income before extraordinary item	\$ 1.13	\$.42
Net income for year	\$ 1.13	\$ 1.55

Consolidated statement of retained earnings

YEAR ENDED DECEMBER 31, 1978 (with comparative amounts for the year ended January 1, 1978)	December 31, 1978	January 1, 1978
Balance, beginning of year	\$ 21,484,576	\$ 20,205,070
Add net income for year	1,517,658	2,086,126
	23,002,234	22,291,196
Deduct:		
Dividends declared (60c per share in 1978 and 1977)—		
Class "A"	541,894	541,894
Class "B"	264,726	264,726
	806,620	806,620
Balance, end of year	\$ 22,195,614	\$ 21,484,576


(See accompanying notes)

Consolidated balance sheet

December 31, 1978 (with comparative amounts at January 1, 1978)

Assets	December 31, 1978	January 1, 1978
Current:		
Cash	\$ 144,258	\$ 264,372
Marketable securities — at cost (approximate market value — \$611,300 at December 31, 1978; \$993,700 at January 1, 1978)	750,000	1,082,671
Accounts receivable	15,628,204	16,022,370
Inventories (note 1(c))	18,868,412	18,497,725
Prepaid expenses	1,113,492	1,460,931
Total current assets	36,504,366	37,328,069
Land, buildings and equipment held for sale (note 1(d))	983,630	1,099,252
Fixed — (notes 1(e) and 2)	27,511,724	29,683,410
Sundry:		
Deferred receivables and other assets	2,000,046	2,816,623
Goodwill (note 1(f))	5,771,229	5,856,553
Expenses in connection with debentures issued, less amortization	167,800	189,800
	7,939,075	8,862,976
	\$ 72,938,795	\$ 76,973,707

On behalf of the Board

 Director

 Director

(See accompanying notes)

Liabilities and shareholders' equity

	December 31, 1978	January 1, 1978
Current:		
Due to bankers (secured by accounts receivable and inventories)	\$ 775,846	\$ 4,364,684
Accounts payable and accrued charges	24,760,794	22,788,489
Income taxes payable	1,285,073	582,690
Dividends declared	201,575	201,575
Principal instalments due within one year (note 3)	1,849,657	2,679,725
	<hr/>	<hr/>
Total current liabilities	28,872,945	30,617,163
	<hr/>	<hr/>
Long-term debt (notes 3 and 5)	12,766,003	14,212,419
	<hr/>	<hr/>
Deferred:		
Income taxes (note 1(g))	1,729,000	2,228,600
Income (note 1(h))	33,916	192,874
	<hr/>	<hr/>
	1,762,916	2,421,474
	<hr/>	<hr/>
Minority interest (note 1(a))		896,758
		<hr/>
Shareholders' equity:		
Capital stock (note 4)	7,341,317	7,341,317
Retained earnings (note 5)	22,195,614	21,484,576
	<hr/>	<hr/>
Total shareholders' equity	29,536,931	28,825,893
	<hr/>	<hr/>
	\$ 72,938,795	\$ 76,973,707
	<hr/>	<hr/>

Consolidated statement of changes in financial position

YEAR ENDED DECEMBER 31, 1978 (with comparative amounts for the year ended January 1, 1978)	December 31, 1978	January 1, 1978
Source of working capital:		
Operations—		
Consisting of:		
Income before extraordinary item	\$ 1,517,658	\$ 561,926
Add (deduct) items not affecting working capital:		
Depreciation and amortization	4,033,604	4,067,602
Deferred income taxes	(392,200)	(754,300)
Minority interest	91,000	149,300
Funds provided from operations	5,250,062	4,024,528
Increase in long-term debt	749,952	2,109,091
Decrease in deferred receivables	700,070	275,232
Net proceeds on disposal of fixed assets	646,162	1,102,342
Proceeds on disposal of investment in Royal Oak Dairy, Limited	\$ 2,050,000	
Less working capital at date of disposal	1,264,951	
	<u>785,049</u>	
	<u>8,131,295</u>	<u>7,511,193</u>
Application of working capital:		
Additions to fixed assets	3,944,716	4,986,615
Repayment of long-term debt	2,158,223	2,800,613
Dividends to shareholders	806,620	806,620
Decrease in deferred income	158,958	167,907
Purchase of goodwill	8,000	104,885
Reductions in minority interest including dividends paid by subsidiary companies	134,263	113,510
	<u>7,210,780</u>	<u>8,980,150</u>
Increase (decrease) in working capital	<u>920,515</u>	<u>(1,468,957)</u>
Working capital, beginning of year	<u>6,710,906</u>	<u>8,179,863</u>
Working capital, end of year	<u>\$ 7,631,421</u>	<u>\$ 6,710,906</u>
Represented by:		
Current assets	\$ 36,504,366	\$ 37,328,069
Current liabilities	28,872,945	30,617,163
Working capital	<u>\$ 7,631,421</u>	<u>\$ 6,710,906</u>

(See accompanying notes)

Notes to the consolidated financial statements

December 31, 1978

1. Summary of significant accounting policies

The consolidated financial statements present the financial position, results of operations and changes in financial position of the company in accordance with generally accepted accounting principles applied on a consistent basis. The more important accounting policies are summarized as follows:

(a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of all subsidiary companies in which Silverwood Industries Limited or its subsidiaries owned an equity interest in excess of 50% at the respective fiscal year ends with appropriate provision for minority interests. Intercompany accounts and transactions have been eliminated.

The results of operations of Royal Oak Dairy, Limited have been included in the attached financial statements for the year 1977 and for the period from January 1, 1978 to the date of sale of that subsidiary company on September 29, 1978 (see note 8).

(b) Definition of fiscal year

The fiscal year of Silverwood Industries Limited for 1978 ended on December 31, 1978 and for 1977 on January 1, 1978, with 1978 comprising 52 weeks and 1977 comprising 53 weeks. The fiscal year for the year ended January 1, 1978 will be referred to as 1977.

(c) Inventories

Inventories are valued at the lower of cost and estimated net realizable value. Cost is determined by the retail method (retail price less normal margin) for convenience stores inventories and the first-in, first-out method for dairy division and supplies inventories.

Inventory values are as follows:

	December 31, 1978	January 1, 1978
Convenience stores	\$ 10,637,366	\$ 10,901,057
Dairy division	3,012,687	2,989,731
Supplies	5,218,359	4,606,937
	<u>\$ 18,868,412</u>	<u>\$ 18,497,725</u>

(d) Land, buildings and equipment held for sale

Discontinued facilities held for sale are carried at the lower of cost less accumulated depreciation or estimated realizable value and are shown as a separate item in the balance sheet.

(e) Fixed assets

Fixed assets are carried at cost. Depreciation and amortization are provided on a straight line basis using rates that will charge operations with the cost of these assets over their estimated useful lives. When fixed assets are sold, the related cost and accumulated depreciation or amortization are removed from the respective accounts and any profit or loss is reflected in the consolidated statement of income. Expenditures for repairs and maintenance are charged to income as incurred. The depreciation and amortization periods are as follows:

Buildings	20 - 50 years
Machinery and equipment	10 years
Merchandising equipment	10 - 12 years
Delivery equipment	7 years
Leasehold improvements	term of lease

(f) Goodwill

Goodwill, arising from the excess of purchase price of subsidiaries over the value of the underlying assets and purchased goodwill, acquired prior to January 1, 1974, is carried at cost, less net proceeds from any disposals. Pre-1974 goodwill has been allocated by management to certain geographic areas. The net proceeds on disposal of goodwill reduce first the cost of goodwill in the related geographic area, then any proceeds in excess of cost are accounted for as an extraordinary item in the income statement.

Goodwill acquired after December 31, 1973 is being amortized on a straight line basis over periods of five to ten years. Amortization for 1978 and 1977 amounted to \$93,300 and \$59,300 respectively.

(g) Deferred income taxes

The company follows the tax allocation method of accounting. The deferrals arise substantially from the company claiming capital cost allowance for income tax purposes in excess of depreciation and amortization charged to consolidated income.

(h) Franchise fees

Franchise fees are taken into income over the term of the franchise agreement on a straight-line basis.

2. Fixed assets

The major categories of fixed assets are as follows:

	December 31, 1978			January 1, 1978
	Cost	Accumulated depreciation	Net book value	Net book value
Land	\$ 1,283,873		\$ 1,283,873	\$ 1,647,628
Buildings	9,351,612	\$ 2,492,651	6,858,961	7,038,025
Machinery and equipment	14,554,430	9,919,016	4,635,414	4,975,363
Merchandising equipment	22,829,826	12,928,308	9,901,518	10,515,510
Delivery equipment	6,153,722	4,619,303	1,534,419	2,262,877
Leasehold improvements	4,861,371	1,563,832	3,297,539	3,244,007
	<u>\$ 59,034,834</u>	<u>\$ 31,523,110</u>	<u>\$ 27,511,724</u>	<u>\$ 29,683,410</u>

3. Long-term debt

	December 31, 1978	January 1, 1978
7-1/4% sinking fund debentures Series A, due July 5, 1986 (sinking fund payment of \$400,000 per annum)*	\$ 5,175,500	\$ 5,597,000
Term notes payable to bankers at prime plus 1% interest, due 1978 to 1982**	8,281,763	10,037,544
8% - 11% mortgages payable	898,152	966,604
Other (lease deposits)	260,245	290,996
	<u>14,615,660</u>	<u>16,892,144</u>
Less portion due within one year included in current liabilities (net of debentures redeemed in advance)	<u>1,849,657</u>	<u>2,679,725</u>
	<u>\$ 12,766,003</u>	<u>\$ 14,212,419</u>

Aggregate non-current maturities and sinking fund requirements are as follows:

Year ended	Amount
December 28, 1980	\$ 2,459,426
December 27, 1981	2,884,603
December 26, 1982	2,291,886
January 1, 1984	554,386
Subsequent years	4,575,702
	<u>\$ 12,766,003</u>

*The sinking fund debentures are secured by a first floating charge on the assets of the parent company and by a specific charge on its real property.

**The assets of two subsidiary companies are pledged under floating charge debentures as security for term notes of these subsidiaries totalling \$7,281,763 which amount is included in the \$8,281,763.

4. Capital stock

The details of the capital stock for 1977 and 1978 are set out below:

Class "A" shares without par value entitled to cumulative, preferential dividends of 60c per share per annum, payable quarterly, and after the Class "B" shares have received 60c per share in any one year to further participation rateably with Class "B" shares; entitled in liquidation to a priority of \$15 per share —
Class "B" shares without par value

	Class "A"	Class "B"	
Authorized	1,000,000 shares	500,000 shares	
Issued	903,158 shares	441,212 shares	\$ 7,341,317

5. Restrictions on payment of dividends

Under the provisions of the Trust Indenture securing the 7-1/4% sinking fund debentures, the company cannot declare or pay dividends (other than stock dividends and dividends at the rate of 60c per share per annum on the outstanding Class "A" shares of the company) when:

(a) consolidated net current assets (as therein defined) of the company and its designated subsidiaries are less than, or would thereby be reduced to less than \$2,500,000 and

(b) the consolidated retained earnings of the company and its designated subsidiaries will be less than the lesser of 75% of the principal amount of all funded obligations of the company and its designated subsidiaries or \$7,500,000.

The company is in compliance with the covenants of the Trust Indenture.

6. Lease agreements and commitments

(a) Lease agreements

Silverwood Industries Limited and its subsidiary companies have entered into agreements to lease equipment and properties for various periods up to 1995 at total maximum aggregate net rentals of approximately \$65,257,000. Minimum annual net rentals which will be charged to consolidated operations in the ordinary course of business in subsequent years for leases in effect at December 31, 1978 are as follows:

December 30, 1979	\$8,895,000
December 28, 1980	8,667,000
December 27, 1981	8,159,000
December 26, 1982	7,646,000
January 1, 1984	7,114,000

Certain of these leases provide for additional rent based on sales.

(b) Pensions

Actuarial estimates of the company's liability in respect of past service pension benefits not provided for in the attached consolidated financial statements amounted to approximately \$584,000 as at December 31, 1978 and \$627,500 as at January 1, 1978. It is the intention of the company to provide for and pay this liability over a period not exceeding the next eleven fiscal years.

The company accounts for current pension costs on an accrual basis and past service costs on a cash basis in accordance with funding recommended by the company's consulting actuaries and as approved under the Pension Benefit Act of Ontario.

7. Extraordinary item — 1977

Gain on sale of discontinued facilities and goodwill less related expenses and deferred income taxes recoverable of \$171,050	\$ 1,524,200
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8. Disposal of subsidiary company

The company disposed of its investment in Royal Oak Dairy, Limited at its carrying value of \$2,050,000 at September 29, 1978. The selling price was satisfied by a cash payment of \$1,621,100 and the issue of 4,289 preference shares of the purchaser. These preference shares were redeemed prior to December 31, 1978 for a cash consideration of \$428,900.

The net income attributable to the operations of Royal Oak Dairy, Limited, after making provision for minority interest, has been included in the attached consolidated statement of income for the 1977 year (\$260,427) and for the period January 1, 1978 to the date of sale on September 29, 1978 (\$177,208).

9. Other statutory information

(a) Remuneration of directors and senior officers

Aggregate direct remuneration paid or payable by the company and its subsidiaries to directors, who act only in that capacity, and senior officers, some of whom act as directors of the company but do not receive additional remuneration as such, as defined by Section 178(11) of The Business Corporations Act of Ontario, amounted to:

	December 31, 1978	January 1, 1978
Directors	\$ 26,100	\$ 23,200
Senior officers	517,876	511,366
	<u>\$ 543,976</u>	<u>\$ 534,566</u>

(b) Classes of business

The company has determined that the classes of business contributing in excess of 10% of sales in 1978 and 1977 were as follows:

	December 31, 1978		January 1, 1978	
	Dollars	Percentages	Dollars	Percentages
Convenience stores	\$176,953,505	60.1%	\$159,705,395	60.1%
Dairies	140,469,563	47.7	131,599,164	49.5
	<u>317,423,068</u>	<u>107.8</u>	<u>291,304,559</u>	<u>109.6</u>
Less inter-company sales	23,081,265	7.8	25,438,030	9.6
Consolidated sales	<u>\$294,341,803</u>	<u>100.0%</u>	<u>\$265,866,529</u>	<u>100.0%</u>

10. Taxes on income

Taxes on income have been reduced by \$246,000 in 1978 and by \$177,000 in 1977 by claiming the 3% inventory allowance as permitted under the amendments to the Income Tax Act, Canada.

11. Anti-inflation program

Under the federal government's anti-inflation legislation (which was in force until December 31, 1978) the company was subject to mandatory compliance with legislation which controlled prices, profit margins, employee compensation and shareholder dividends.

Management is of the opinion that the company is in compliance with the requirements of the anti-inflation legislation.

Mac's



R. S. Maich
President



R. F. Egerdie
Vice President, Finance



E. C. Higgins, Vice President,
Corporate Development



R. C. Broadhead, Vice President,
Merchandising



B. Livingston, Vice President,
Real Estate



J. DeWit, Vice President,
Ontario Operations



R. Pylypiw, Vice President,
Western Operations

Mac's Convenience Stores Limited continued its leadership of the Canadian Convenient Store industry achieving record sales and profitability in 1978. The overall profitable growth of the Company and its network of independent dealers across Canada was a result primarily of the increasing market share per store. Our performance during the year was broadly based in virtually all Mac's markets and indicated the continued responsiveness of our consumer strategies to the present and future needs of our customers.

There were 602 stores in operation at the end of 1978 as compared to 594 stores at the year end 1977. There were 46 new quality locations opened while 38 outlets no longer viable for the short and longer term future were closed. Seventeen of those closings were in the Province of Quebec where a total re-evaluation of our marketing posture has taken place.

Record sales of \$166,710,297 had grown by \$20,009,146 or 13.6% over the previous year. It should be noted that this increase is well in excess of the inflation rate within the Canadian economy and has been accomplished with only a 2% increase in store count. It should also be remembered that Mac's does not participate in sales of fresh meat or fresh fruits and vegetables. These products were the prime cause of the inflationary price record of foods in Canada during 1978.

Operating in five provinces, Mac's management has continued to be challenged by five different economic and political climates. Average sales per store increased significantly in all markets with market share being gained in Ontario, Manitoba and Alberta.

At year end, there were 406 stores in Ontario, 30 in Manitoba, 78 in Alberta, 61 in British Columbia and 27 in Quebec.

The Company's newest market, Quebec, continued in its developmental phase with major actions taking place during 1978 to rationalize the store base to a nucleus of outlets with short and longer term return on investment potential. The aggressive assessment of individual store potentials resulted in disposal of some 17 locations during 1978. Average sales per store increased on those remaining, even though Mac's franchisees do not have the benefit of the beer or wine distribution enjoyed by many convenient store competitors in the Province of Quebec.

With the foundation of industry leadership, record sales and profits, Mac's is most optimistic regarding both the short and long term future. During 1978 a multitude of new concepts were developed and initiated into prototype and test marketed throughout Canada. New product categories are being introduced in selected Canadian markets including Mac's Fast Snacks, Photo-centres, Reading Centres and other non-food items. Gasoline retailing is being undertaken in many store units while prototypes of a cluster concept integrating the new Mac's store of the future plus a selection of compatible business concepts such as delicatessen, wine stores and in-store bakeries are now in operation for test purposes.

The year 1978 was outstanding for Mac's Convenience Stores Limited and reflects the strength of the convenience store concept, its independent and entrepreneurial dealer network and the dedication, ambition and innovation of personnel throughout the Mac's team.

Baskin-Robbins



T. G. Bryant
Regional Director



C. F. Findlay, Manager,
Real Estate Division



D. G. Seebach
Franchise Manager



R. C. Newton
District Representative

The Baskin-Robbins franchise continues to provide small business opportunities for many Canadians. Currently, there are sixty-one independent Baskin-Robbins store owners within Ontario who are living examples that free enterprise is alive and well. These individual proprietorships or multiple store family business units, are combining their entrepreneurial skills with the fun and flavour marketing strengths of Baskin-Robbins 31 Ice Cream, to achieve their personal goals.

The outstanding consumer acceptance for the high quality Baskin-Robbins product line continues to be demonstrated both in the metropolitan markets and the smaller communities expanded into during 1978. Baskin-Robbins retail ice cream stores extend as far east as Ottawa and as far west as Windsor and include many smaller communities such as Guelph, Waterloo, Kingston, Barrie, Belleville, Grand Bend, Cobourg, Chatham, Sarnia and Woodstock.

During 1978, eleven new stores were opened within the Province of Ontario. These new stores, along with favorable weather conditions, contributed to a 30.3% increase in total ice cream sales in Baskin-Robbins stores. In addition to this growth in numbers of retail outlets and total ice cream sales, the Baskin-Robbins Division has acquired the franchise rights for the entire Canadian market.

The adherence to high standards of product and performance at the retail level and a spirit of excellence within the Baskin-Robbins Division has and will continue to play an important role in our goal of achieving the position of leadership in the industry.



M. E. Duffy
President



R. C. Ferguson, Vice President,
Finance and Administration



P. B. Knoepfli, Vice President,
Planning and Marketing



W. M. Hadwell, Vice President and
General Manager, Western Division



W. W. Pascoe, Director of
Plant Operations



D. E. Coe
Manager, Toronto District



T. F. Kotschorek
Manager, London District

Silverwood Dairies

Significant changes have been taking place within our Dairy Food operation across Canada in 1978, and although this Division remained unprofitable for the fiscal period, sales trends are much improved and a return to profitability is anticipated in 1979. As has been indicated, the major weakness remains in the highly competitive and ever changing Ontario marketplace.

Sales for 1978 were \$129,978,591, an increase of \$9,226,025 or 7.6% over 1977, a distinct improvement from the sales performance of the previous two years. The shorter fiscal period of 1978 would alter comparison by approximately 2%.

Ice cream sales and profitability were disappointing throughout the total market, despite very favourable weather conditions particularly in the Eastern part of the country. It is evident the general economic conditions, changing patterns of food consumption and dietary considerations are impacting the sales growth of this nutritious food product. Silverwood continues to lead the market in the production and sale of premium quality lines with its Canadian Supreme, Canadian DeLuxe, Laura Secord and Baskin-Robbins Ice Creams. We remain adamant in our attitude that much harm is being done to the potential of a fine Canadian food by other manufacturers and retailers in the encouragement of low quality, lower price ice cream consumption among Canadians.

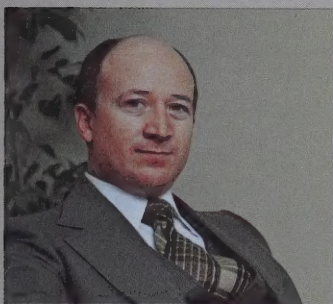
The markets of Vancouver and Victoria in British Columbia remain strong both in sales performance and profit contributions particularly in the fluid milk field. In Manitoba we are encouraged by increasing dairy sales and profit contribution, arising out of capital expenditures in the plant facilities made some six to seven years ago. Thus, Silverwood Dairies is growing and increasing its market share in those sectors of Western Canada in which it participates.

Ontario remains an ever changing enigma. The fluid milk and ice cream operating margins are constantly under attack because of the extremely competitive conditions which exist within the market. The major retailers, being few in number, exert an extremely powerful influence over volume sales and consequently volume production and costs in their own competitive food marketplace. Fluid milk is constantly being used as a loss leader to attract consumers. In the short run, there can be no question that the Canadian consumer benefits immeasurably from these practices. In the long run, depressed conditions for food processors may well lead to a weakened independent food industry or a highly verticallized and powerful retailing sector.

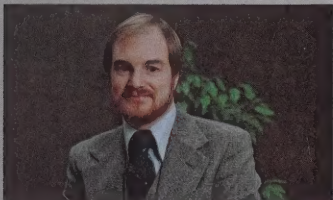
The Silverwood dairy product enjoys wider distribution than that of any other dairy in Canada, and we service a significant and growing section of medium-sized retail outlets and the newly emerging independent chains. It is significant to note that no single customer represents more than 6% of our business and, therefore, we are not vulnerable to any single customer or group of customers.

With these conditions, Silverwood Dairies has had to develop a much leaner, efficient operating structure to survive. Every effort is being made to eliminate costly selling and distribution practices which have been a part of the industry for many years. In so doing, we recognize that the gross margins of the small retailer in dairy products are under attack and that this segment of the market will continue to decline.

Emphasis will continually be placed on altering the position of Silverwood within the marketplace with practices which will enable it to compete for a greater share of the consumer's dairy food dollar.



W. L. Wilson
General Manager



P. Barker
Accountant



D. T. Sansone
Production Supervisor

Londonderry

Londonderry Distributors Limited, the wholly owned aseptic citrus juice processing plant of Silverwood Industries Limited, had a rewarding year in both sales and profitability. Sales in aseptic citrus juice increased by 23.8% to \$3,709,910. This occurred in spite of the highly competitive nature of the market and the marked softness in industry sales. This softness can be attributed to the substantial increase in citrus concentrate costs, the dramatic decline of the value of the Canadian dollar vis-a-vis the U.S. dollar, and increases in labour and packaging costs.

However, the Company showed a significant increase in operating income due to dramatic increases in production efficiencies and a stringent and timely pricing policy. A cost conscious management tightened control of expenses allowing profitability to return to this division in a more adequate fashion.

In 1979, orange concentrate costs are expected to stabilize, resulting in only marginal increases in finished product pricing. This should result in some improvement in total orange juice consumption. It is expected that several new purchasing concepts in citrus juices will be introduced to the market in 1979 by both Londonderry and its competitors. We expect to expand our product line with the introduction of lemonade, fruit punch, grape juice and grape drink, as well as a vegetable cocktail product.

It is the intention of the management of the Company to develop and market new concepts and techniques which will help diversify our business and open new markets essential to the ongoing growth of the Company.



A. G. Sargent
Director

Research & Development

The Research and Development laboratory is a corporate resource established and maintained under the guidance and control of Silverwood Industries Limited, as a technical support function to all Company divisions.

The offices, laboratory and pilot plant facilities are located in London, Ontario, and operates with a highly trained technical staff having backgrounds in the fields of food science, chemistry and microbiology, assisted by support technologists. The objectives are both to investigate and initiate technological innovations and product improvements that will contribute to the marketing growth and processing efficiencies of the operating subsidiaries of Silverwood Industries Limited.

Over the years, the National Research Council of Canada has provided assistance and technological advice in conjunction with our R & D laboratory involvement in applied research projects.

General Information

Operating Divisions

Silverwood Dairies Limited

Head Office, Toronto, Ontario

President — M. E. Duffy

Vice President, Finance and Administration — R. C. Ferguson

Vice President, Planning and Marketing — P. B. Knoepfli

Vice President and General Manager, Western Division — W. M. Hadwell

Director of Plant Operations — W. W. Pascoe

Manager Toronto District — D. E. Coe

Manager London District — T. F. Kotschorek

Baskin-Robbins 31 Flavour Ice Cream Stores

Toronto, Ontario

Regional Director — T. G. Bryant

Manager Real Estate Division — Craig F. Findlay

Franchise Manager — D. G. Seebach

District Representative — R. C. Newton

Mac's Convenience Stores Limited

Head Office, Toronto, Ontario

President — R. S. Maich

Vice President, Finance — R. F. Egerdie

Vice President, Corporate Development — E. C. Higgins

Vice President, Merchandising — R. C. Broadhead

Vice President, Real Estate — B. J. Livingston

Vice President, Ontario Operations — J. DeWit

Vice President, Western Operations — R. J. Pylypiw

Research & Development

London, Ontario

Director — A. G. Sargant

Londonderry Distributors Limited

Toronto, Ontario

General Manager — W. L. Wilson

Accountant — P. Barker

Production Supervisor — D. T. Sansone

Kayesil Limited

Head Office, London, Ontario

Corporate Data

Head Office

75 Bathurst Street,

London, Ontario N6B 1N8

Mailing Address

P.O. Box 2185,

London, Ontario N6A 4E5

Transfer Agents

The Canada Trust Company

Toronto, Calgary and Vancouver

Auditors

Clarkson, Gordon & Co.

Chartered Accountants

Silverwood Industries Limited
75 Bathurst Street, London, Ontario N6B 1N8